

## Message Text

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ORIGIN OPIC-06

INFO OCT-01 NEA-10 ISO-00 EB-07 AID-05 OMB-01 TRSE-00 /030 R

DRAFTED BY OPIC/D:JCDILL:PLD

APPROVED BY EB/IFD/OIA:RJSMITH

EB/IFD/OIA:DHSTEBBING

NEA/EGY:GRBEYER (INFO)

----- 084039

R 020053Z MAR 76

FM SECSTATE WASHDC

TO AMEMBASSY CAIRO

UNCLAS STATE 050077

PASS TO D. GREGG, OPIC/EVP (ETA CAIRO 3-6-76)

E.O. 11652: N/A

TAGS: OVIP TRV SIMON

SUBJECT: FOREIGN EXCHANGE SAVINGS FROM IMPORT SUBSTITUTION

1. THE WORLD BANK, IN JUDGING THE ECONOMIC RETURNS FROM AID TO PROJECTS IN DEVELOPING NATIONS, MUST CONSIDER THE HOST COUNTRY ADVANTAGES IN SAVINGS OF FOREIGN EXCHANGE FROM IMPORT SUBSTITUTION PROJECTS. THE SAVINGS OF SUCH A PROJECT ARE MOST SIGNIFICANT WHEN THE PRODUCT IS AN ESSENTIAL COMMODITY WHICH, ALONG WITH ITS POSSIBLE SUBSTITUTES, IS IN SHORT SUPPLY IN THE DOMESTIC MARKET. IN THIS CASE THE FOREIGN EXCHANGE SAVINGS CAN BE ESTIMATED FROM THE LANDED COST C.I.F. OF AN IMPORT OF THE SAME COMMODITY; LESS THE LANDED COST OF IMPORTED COMPONENTS, RAW OR SEMI-FINISHED MATERIALS REQUIRED FOR ITS PRODUCTION; LESS PAYMENTS OF INTEREST, ROYALTIES, FEES, AND LOAN PRINCIPAL; LESS DEPRECIATION; AND FINALLY DEDUCTING A REASONABLE RETURN ON CAPITAL INVESTED. WHETHER THE ACTUAL AUDITED PROFITS SHOULD BE FULLY CREDITED AS A FOREIGN EXCHANGE SAVINGS DEPENDS ON WHETHER IT CONTAINS WINDFALL BENEFITS FROM, FOR EXAMPLE, TARIFF LEVELS WHICH ARE EXCESSIVE FOR PURPOSES OF PRO-  
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TECTING THE VIABILITY OF THE INDUSTRY.

2. FOREIGN EXCHANGE SAVINGS WOULD BE LESS THAN THE RESULT OF THE PRECEDING CALCULATIONS TO THE EXTENT THAT THE FOLLOWING CONSIDERATIONS ALSO PLAY A ROLE:

----IF THE NEW PROJECT PRODUCES A PRODUCT WHICH DEPENDS ON A BRAND NAME OR OTHER MEANS OF DIFFERENTIATING IT FROM SIMILAR OR SUBSTITUTE PRODUCTS ALREADY AVAILABLE IN THE DOMESTIC MARKET;

----IF THE PROJECT DEPENDS ON LOCAL ADVERTISING OR OTHER MEANS OF STIMULATING DEMAND ABOVE LEVELS WHICH WOULD HAVE EXISTED IN THE ABSENCE OF THESE EFFORTS.

3. THUS, IF THE GOVERNMENT PLACES HIGH PRIORITY ON A PROJECT TO PRODUCE A PRODUCT WHICH IS BOTH HOMOGENOUS IN NATURE AND AN ESSENTIAL ELEMENT OF EXISTING CONSUMPTION NOT SATISFIED BY DOMESTIC PRODUCTION, THERE SHOULD BE A STRONG PRESUMPTION THAT THE FOREIGN EXCHANGE SAVINGS, INCLUDING PROFIT, WILL CORRESPOND CLOSELY TO THE FOREIGN EXCHANGE SAVINGS OF THE ECONOMY AS A WHOLE. EARMARKING OR OTHER ALLOTMENT OF FOREIGN EXCHANGE RESERVES TO PERMIT REPATRIATION OF DEBT, ROYALTY, LICENSE, AND EARNINGS PAYMENTS WOULD BE FULLY WARRANTED, UNLESS UNUSUAL FACTORS WERE INVOLVED. MEASURES TO LIMIT FOREIGN EXCHANGE ALLOTMENTS FOR THESE PURPOSES WOULD APPEAR MORE JUSTIFIED IN PROJECTS WHERE THERE IS STRONG PRESUMPTION OF TARIFF-BASED WINDFALL EARNINGS, SUBSTITUTION FOR DOMESTIC PRODUCTION OF IDENTICAL OR COMPETING PRODUCTS, AND ELEMENTS OF MARKET CREATION THROUGH ADVERTISING OR OTHER DEMONSTRATION EFFECTS.

4. WE WILL COMPARE THESE JUDGMENTS WITH WORLD BANK OFFICIALS TO DETERMINE WHETHER THE CRITERIA ARE SIMILAR TO THOSE USED BY THE BANK. IN MY OBSERVATIONS AND EXPERIENCE TO DATE, I WOULD EXPECT CLOSE SIMILARITY OF THE ABOVE TO BANK CRITERIA.

5. PRECEDING FOUR PARAGRAPHS TEXT OF MEMO TO YOU FROM E. HEGINBOTHAM. INGERSOLL  
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## Message Attributes

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**Capture Date:** 01 JAN 1994  
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